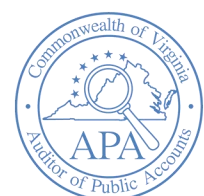




DEPARTMENT OF VETERANS SERVICES
VETERANS SERVICES FOUNDATION

REPORT ON AUDIT
FOR THE PERIOD
JULY 1, 2012 THROUGH DECEMBER 31, 2014

Auditor of Public Accounts
Martha S. Mavredes, CPA
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AUDIT SUMMARY

Our audit of the Department of Veterans Services (Veterans) for the period July 1, 2012, through December 31, 2014 and the Veterans Services Foundation as described in the section entitled “Audit Scope and Methodology,” found:

- proper recording and reporting of all transactions, in all material respects, in the agency financial system;
- matters involving internal control and its operation necessary to bring to management’s attention;
- instances of noncompliance with applicable laws and regulations or other matters that are required to be reported; and
- an other matter in a “Comment to Management” for the Commissioner of Veterans.

–TABLE OF CONTENTS–

	<u>Pages</u>
AUDIT SUMMARY	
COMMENT TO MANAGEMENT	1
FINDINGS AND RECOMMENDATIONS	2-8
INDEPENDENT AUDITOR’S REPORT	9-11
AGENCY RESPONSE	12-13
AGENCY OFFICIALS	14

COMMENT TO MANAGEMENT

Why the APA is Reporting a Comment to Management for Payroll

Payroll is Department of Veterans Services' largest expenditures category at approximately \$34 million (62 percent) annually. During the course of our audit, we learned of Veterans' dissatisfaction with the payroll services provided from the Department of Accounts' (Accounts) through its Payroll Service Bureau and Accounts' concerns with the controls over payroll at Veterans. Instead of executive management at both agencies, Veterans and Accounts, collaborating to the level needed to resolve any issues, the Commissioner of Veterans has decided to terminate Veterans' relationship with Accounts. We offer the following comment to management to ensure they properly evaluate the situation and make the decisions needed to ensure that payroll, their largest expenditure, is properly controlled in the future.

Evaluate Payroll Controls and Capabilities before Terminating Service Agreement

Veterans uses Accounts' Payroll Service Bureau (Bureau) for payroll processing, leave accounting, and reconciliations and information returns. Veterans requested that the service agreement between Veterans and the Bureau be terminated. If terminated, Veterans will be responsible for operating controls and functions currently provided by the Bureau. Under the service agreement, the Bureau provides payroll functions for Veterans and a layer of controls for the Commonwealth to ensure that Veterans' payroll is accurate and complies with state and federal requirements.

Before terminating the service agreement, the Commissioner of Veterans should evaluate if the agency has the capabilities to develop and implement the functions and controls currently provided by the Bureau. In making this determination, we encourage the Commissioner to have an open dialog with the State Comptroller about the functions and, more importantly, the controls that the Bureau is providing as part of the service agreement. If, after consultation and careful consideration, the Commissioner of Veterans still desires to proceed with the termination of the service agreement, Veterans will need to fund and properly plan for its development, implementation, and testing of the functions and controls previously provided by the Bureau.

FINDINGS AND RECOMMENDATIONS

Why the APA Reviews Financial Operating Procedures

Veterans operates in a decentralized environment. It manages two care centers and a central office, with each responsible for controlling its own financial transactions. However, the central office is responsible for establishing and monitoring the controls across the entire organization. To evaluate if the Central Office has communicated its control expectations agency-wide and has the information needed to perform its own review of controls, we reviewed procedures from across the organization. Our review of operating procedures resulted in the following recommendation for Veterans to provide more details within its procedures to strengthen its control environment.

Strengthen Detailed Standard Operating Procedures for Reconciling Financial Related Systems

Veterans does not have adequate written procedures governing its reconciliations between the Fixed Asset Accounting and Control System (FAACS) and the Commonwealth Accounting and Reporting System (CARS). Veterans' current written procedures do not properly address the specific positions involved in the reconciliation process, the timeframe of the reconciliation, or how to incorporate the Commonwealth Accounting Policies and Procedures (CAPP) Manual's reconciliation template into the agency's monthly FAACS to CARS reconciliation.

CAPP Manual, Topic 20905: CARS Reconciliation Requirements, requires that "agencies must have detailed written procedures for meeting all CARS reconciliation requirements. These "desk procedures" must require documenting reconciliations in an agency-standardized format and making them available for inspection (with all supporting documentation) by outside parties such as the Auditor of Public Accounts (APA) and the Department of Accounts (DOA)."

The lack of detailed desk procedures for FAACS to CARS reconciliations increases the risk of error in CARS, which is the Commonwealth's official financial system. The increased risk of error can be caused by one or more of the following: reconciliations not being performed in sufficient detail to allow for their review, approval, and audit; employees who are unaware of their reconciliation responsibilities and the timeframe for completing these reconciliations; responsibilities for reconciliations not being transferred when there is employee turnover; and/or management not being able to hold employees accountable when they do not perform reconciliations as required. The lack of desk procedures for CARS reconciliations was brought to management's attention during two prior audits. In response, Veterans created desk procedures governing reconciliations for financial systems; however, the FAACS to CARS reconciliation procedures do not include enough detail to reduce the aforementioned risks.

Management at Veterans should revise and implement detailed written procedures in an agency-standardized format for employees to follow in confirming that each of its financial related systems reconcile to each other to ensure their accuracy. These procedures should clearly identify

the positions responsible for each part of the reconciliation, the timing of the reconciliation, and the source documents and format for the reconciliation.

Why the APA Audits Supervisor Approvals for Payroll and Controls Over the Virginia Retirement System Reconciliation Process

As stated previously, payroll is Veterans' largest expenditures category at approximately \$34 million (62 percent) annually. As a result of the significance of payroll and related activities, we evaluate controls that management uses to ensure that a supervisor approves each employee's time for the actual hours worked. Additionally, we tested the controls surrounding Veterans' submission of information to the Virginia Retirement System that is used to determine benefits for each employee. Our work in these areas resulted in the following two recommendations for management.

Ensure a Supervisor Approves Each Time and Attendance Record

Veterans' Sitter and Barfoot Veterans Care Center (Sitter and Barfoot) does not have adequate segregation of duties within its time and attendance system, Kronos, to prevent managers from approving their own time cards. A review of time card approvals at Sitter and Barfoot during the audit period identified 13 instances where a manager approved their own time card without a subsequent review and approval by an appropriate supervisor.

Approval of time cards is a critical control that provides evidence that services were received and reasonable, and that time worked is accurate. An appropriate supervisor should review and approve each employee's time card. The absence of proper internal controls over the recording of hours worked increases the risk for the following issues:

- Paying for hours that were not worked
- Paying for excessive overtime, including shift differentials
- Not reducing leave balances for hours not worked

Kronos has a limited number of manager licenses available, and managers can only view and approve time cards of employees they supervise. Consequently, when a manager is absent, the backup manager may need to approve their own time card in order to facilitate timely payroll processing. In response to a prior audit recommendation concerning time card approval, Sitter and Barfoot changed protocol to create a compensating control over time card approval. If a manager is absent for time card approval, a backup manager approves those time cards to facilitate timely payroll processing. When the primary manager returns, they must retroactively review and approve time cards for the period of their absence. For the time cards in question, a backup manager approved their own time during the primary manager's absence, but the primary manager did not perform a retroactive review of these time cards to ensure that the employees accurately recorded their time and leave. Although Sitter and Barfoot created procedures to address the prior audit

recommendation, management has not documented these procedures in the time and attendance policy.

Management at Sitter and Barfoot, if they agree with the procedures after the last audit, should incorporate them into the documented policy, train managers, and ensure that managers are following the time card approval procedures.

Improve Controls over the Virginia Retirement System Reconciliation Process

Veterans and its Care Centers do not have documentation to support reconciliations performed between myVRS Navigator and the Personnel Management Information System (PMIS). Additionally, Veterans did not provide its employees with written policies and procedures for performing the reconciliation. Without this documentation, management was not able to substantiate and we were unable to verify that Veterans and its Care Centers perform adequate procedures to ensure that retirement information is accurate prior to management's certification of the monthly Virginia Retirement System Contribution Snapshot.

Furthermore, Veterans does not have adequate internal controls to ensure timely certification of its monthly retirement Contribution Snapshots. During the period of January 2013 through December 2014, Veterans headquarters did not certify 15 of 24 (63 percent) Contribution Snapshots within the required time frame. Additionally, the Virginia Veterans Care Center did not certify five of 24 (21 percent) Contribution Snapshots within the required time frame. Agency certification of the retirement Contribution Snapshot became a statewide requirement as of January 2013; however, for the period of January 2013 through July 2014, management could not determine who performed these certifications in the myVRS Navigator system for Veterans headquarters and the Virginia Veterans Care Center.

CAPP Manual Topic 50410 requires each agency to certify retirement contributions monthly through a "snapshot" of the agency's expected contribution in total and by member, based on the data in myVRS Navigator at the time of the snapshot. As stated in CAPP Manual Topic 50410 and the Accounts Payroll Bulletin Volume 2013-02, agencies must certify the Contribution Snapshot no later than the tenth of the month following the month being certified. Certification activities reasonably can begin as early as the 25th day of the month being certified; since this is the day immediately following the end of the month's second pay period, the agency would have accurate data to certify as of this date.

This certification becomes the official basis for the billing of retirement contributions and the payable due from the agency. As stated in Accounts' Payroll Bulletin Volume 2013-02, careful review of the monthly Contribution Snapshot is critical to the accuracy of the retirement system reconciliation. To ensure the accuracy of member data and members' retirement contributions, the agency must ensure that myVRS Navigator, PMIS, and the Commonwealth Integrated Payroll and Personnel System (CIPPS) remain synchronized by promptly updating information and thoroughly reconciling data between all three systems.

The Bureau performs the payroll functions for Veterans and its Care Centers and completes some of the reconciliation functions between myVRS Navigator and CIPPS, including keying corrections in CIPPS. However, the Payroll Service Bureau is unable to determine the completeness and accuracy of the agencies' payroll and cannot key corrections into the myVRS Navigator system; therefore, Veterans and its Care Centers are responsible for these functions of the reconciliation. Additionally, CIPPS retirement plan information is updated by the interface between myVRS Navigator and CIPPS; therefore, to ensure accurate data in all three systems and prevent exception items on automated reports generated after the Snapshot certification, Veterans and its Care Centers should research and correct any variances between myVRS Navigator and PMIS prior to certifying the Contribution Snapshot.

Since myVRS Navigator, PMIS, and CIPPS share the data elements that are the basis for the retirement contribution calculation, certifying the Contribution Snapshot without researching existing variances can cause errors in members' retirement related data and can lead to an agency underpaying or overpaying retirement contributions to the Retirement System, creating complications when a member retires. Additionally, without written policies and procedures employees are not provided with sufficient guidance needed to perform the procedures necessary to reconcile retirement contribution data and certify the monthly retirement Contribution Snapshot.

Furthermore, once an agency certifies the Contribution Snapshot, it becomes the official basis for the Virginia Retirement System billing amount. Accounts performs a high-level reconciliation of CIPPS and myVRS Navigator and then processes an Interagency Transfer for the differences. Accounts cannot perform this high-level reconciliation until all CIPPS agencies confirm the contributions, and therefore, the entire process is delayed if a single agency does not confirm the contribution by the required deadline.

In fall 2012, the Virginia Retirement System launched the myVRS Navigator system, which significantly changed the member data collection and retirement contribution reporting process, as well as the retirement reconciliation process. The timing of the implementation of myVRS Navigator closely aligned with Veterans' transition to using the Payroll Service Bureau to perform its payroll functions as of July 1, 2012. Since implementing myVRS Navigator, the Virginia Retirement System, Accounts, and the Bureau have issued guidance to agencies about changes in the retirement reconciliation process; this guidance is separated into numerous publications and correspondence from multiple agencies. Management at Veterans and its Care Centers has not adequately assessed this statewide guidance to develop a clear understanding of the agencies' current responsibilities for the monthly retirement reconciliation process. As a result, Veterans and its Care Centers do not have a written policy that details their required retirement reconciliation procedures and assigns reconciliation tasks to the appropriate employees.

Using statewide guidance issued by the Virginia Retirement System, Accounts, and the Bureau, Veterans should create and implement agency-specific policies and procedures for its monthly retirement reconciliation process. These policies should include the time frame for performing retirement reconciliation procedures and clearly define Veterans' responsibilities versus those of the Bureau. Furthermore, these policies should assign the agency responsibilities to

appropriate employees within Veterans and each of the Veterans Care Centers. Veterans' management should ensure that the employees responsible for the monthly retirement reconciliation process are aware of their responsibilities and adequately trained to perform these duties. Lastly, Veterans should retain and review supporting documentation for each reconciliation as evidence that staff performed the procedures and that management subsequently reviewed and approved it prior to its certification.

Why the APA Audits Controls Over Information Systems

Veterans uses multiple systems to manage and control its daily operations. Given the nature of Veterans' operations, many of its systems house sensitive information. As a result, it is important for management at Veterans to control access to ensure it is properly restricted, evaluate external service providers to ensure they are meeting the Commonwealth Security Standards, and provide everyone with security awareness training to ensure users are aware of their responsibilities. Our work in these areas resulted in the following three recommendations for management.

Apply Access Management Policies to Internal Systems

Veterans does not apply its policies and procedures for managing system access to its internal systems. Furthermore, Veterans does not have documentation supporting user access changes made within these systems. In a sample of 30 users with access to Benevets, Financial Management System II, and Point Click Care, Veterans does not have approved access request forms for 27 users (90 percent) or adequate documentation to show that it removed system access in a timely manner for nine users (100 percent of terminated users tested).

The Commonwealth's Information Security Standard, SEC 501-09, (Security Standard), Section AC-1, Access Control Policy and Procedures, requires Veterans to develop, document, and disseminate to all organization personnel an access control policy and procedures to facilitate the implementation of that policy. Additionally, Section AC-2, Account Management, requires Veterans to have appropriate approvals for establishing, activating, modifying, disabling, and removing accounts.

A lack of consistent application of policies and procedures for managing system access increases the risk that system owners inappropriately authorize, create, or modify user accounts. A user with inappropriate access can create unauthorized transactions or gain access to sensitive Commonwealth data.

Veterans' policy 2.01, Physical/Logical Security Access Authorization, includes a Security Access Authorization Form "used to authorize or change access to any Department of Veterans systems, applications, computers, and to request 'new user' account creation." Furthermore, the policy acknowledges that Veterans and the Commonwealth of Virginia "require Physical/Logical Security Access Authorization forms to ensure Information Systems security at all levels and all

locations.” However, Veterans does not apply this policy to internal applications. Veterans’ Chief Information Security Officer delegates access management for internal systems to the system owners, but they are not aware of the Security Standard requirements.

Veterans should develop access management policies and procedures that align with the Security Standard and apply them to all systems, including internal systems. Once the policies and procedures are developed and approved, Veterans should provide training to all system owners to ensure they are aware of their responsibilities for access management in accordance with the Security Standard.

Improve Oversight of Third-Party Providers

Veterans does not obtain and review Service Organization Control (SOC) reports to evaluate the adequacy of information technology (IT) controls at its third-party providers that manage and process its data. Additionally, Veterans’ contracts do not contain language that require third-party providers to supply it with SOC reports on a periodic and ongoing basis for evaluation. Veterans has outsourced several of its sensitive mission critical business functions, including its benefits eligibility application, which is used to process all veterans’ eligibility claims.

The Security Standard considers third-party providers as organizations that perform outsourced business tasks or functions on behalf of the Commonwealth. Section 1.1 of the Security Standard recognizes that agencies may procure IT equipment, systems, and services from third-party providers. In these situations, the Security Standard requires that agencies enforce the requirements outlined in the Security Standard through documented agreements with the third-party providers. One common practice for providing oversight and assurance is to request and review a SOC report from the associated third-party provider.

By not receiving and evaluating SOC reports, Veterans cannot validate and gain reasonable assurance that their third-party providers have implemented effective IT controls to adequately protect its sensitive mission critical data sets. Without the information available within the SOC report, Veterans is not able to provide reasonable assurance that internal controls over the stewardship of the Commonwealth’s assets, data at the service organization, are operating effectively and that there are no significant weaknesses in the design or operations in the related internal controls. Without reasonable assurance, Veterans may unknowingly be jeopardizing the confidentiality, integrity, and availability of its sensitive mission critical information.

Veterans has not requested and reviewed third-party provider SOC reports because it has not established a formal process in its information security program for identifying third-party service providers and providing appropriate oversight. Additionally, Veterans’ third-party provider contracts do not have established language requiring SOC reports.

Veterans should develop a formal process to request and review SOC reports and add language to their contracts requiring third-party vendors to provide them on an ongoing basis. Veterans should also evaluate the complementary controls listed in the SOC reports. After Veterans

develops a formal process to receive and review SOC reports, they should incorporate it into their information security program.

Improve Information Security Awareness Training Program to Meet Required Standards

Veterans' security awareness training program does not meet the requirements in the Security Standard, and Veterans is not monitoring or enforcing employee compliance with its current program.

The Security Standard, Section AT-1, requires that Veterans at least annually develop, disseminate, and review/update a formal, documented security awareness and training policy. The security awareness and training policy must address: purpose, scope, roles, responsibilities, management commitment, coordination among organizational entities, and compliance. The Security Standard further requires Veterans to have formal, documented procedures to facilitate the implementation of the security awareness training policy and compliance monitoring.

Not having formal policies and training procedures that meet all of the Security Standards increases the risk of users not being able to appropriately identify, prevent, and respond to a variety of security threats such as phishing and social engineering, which can result in the compromise of confidential and mission critical systems and data. Additionally, without a formal policy, management may be limited in its ability to monitor employee compliance and hold those accountable that are not practicing sound security practices.

Veterans currently uses multiple training systems, including the Commonwealth of Virginia Knowledge Center (Knowledge Center), to provide its current security awareness training program. Turnover in key positions caused Veterans to have issues utilizing the system and not be effectively enforcing security awareness training and monitoring for policy compliance.

Veterans should develop policies and procedures to align with the Security Standard requirements and develop a more effective process to monitor compliance for all employees, including employees that utilize the Knowledge Center. Once complete, Veterans should incorporate the new processes and controls into the existing information security program. Veterans should contact Knowledge Center administrators to receive training on the system's functionality and determine if the system fulfills their needs. Veterans should also research and evaluate using one comprehensive system to provide effective security awareness training and enable more efficient compliance monitoring.



Martha S. Mavredes, CPA
Auditor of Public Accounts

Commonwealth of Virginia

Auditor of Public Accounts

P.O. Box 1295
Richmond, Virginia 23218

October 21, 2015

The Honorable Terence R. McAuliffe
Governor of Virginia

The Honorable John C. Watkins
Chairman, Joint Legislative Audit
and Review Commission

We have audited the financial records and operations of the **Department of Veterans Services (Veterans)** for the period July 1, 2012, through December 31, 2014, and the **Veterans Services Foundation** as described in the section entitled "Audit Scope and Methodology." We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Audit Objectives

Our audit's primary objectives were to evaluate the accuracy of recorded financial transactions in the Commonwealth Accounting and Reporting System and Veterans' Financial Management System, review the adequacy of Veterans' internal controls, and test compliance with applicable laws, regulations, contracts, and grant agreements.

Audit Scope and Methodology

Veterans' management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws, regulations, contracts, and grant agreements.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered significance and risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

Payroll

Interactions with Payroll Service Bureau

Information provided to the Virginia Retirement System

Small purchase charge card

Personal vehicle travel expenditures

Expenditure voucher processing

Capital outlay

Patient revenues

System access

Management's usage of SSAE 16 reports (SOC Reports)

IT security awareness and training

Veterans Services Foundation

Receipt and disbursement of funds for the period July 1, 2013, through December 31, 2014

Our audit did not include, for the fiscal year ended June 30, 2013, the Veterans Services Foundation and the Veterans State Nursing Home Care Grant, which we audited previously and reported in the Veterans Services Foundation and Veterans State Nursing Home Care Grant at the Department of Veterans Services Report dated January 29, 2014.

We performed audit tests to determine whether Veterans' controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws, regulations, contracts, and grant agreements. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of Veterans' operations. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

Conclusions

We found that Veterans properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System and Veterans' Financial Management System. Veterans records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted certain matters involving internal control and its operation and compliance with applicable laws, regulations, contracts, and grant agreements that require management's attention and corrective action. These matters are described in the section entitled "Findings and Recommendations."

Exit Conference and Report Distribution

We discussed this report with management on October 14, 2015. Management's response to the findings identified in our audit is included in the section titled "Agency Response." We did not audit management's response and, accordingly, we express no opinion on it.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

GDS/alh



COMMONWEALTH of VIRGINIA

Department of Veterans Services

John L. Newby II
Commissioner

Telephone: (804) 786-0286
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October 21, 2015

Martha S. Mavredes
Auditor of Public Accounts
P. O. Box 1295
Richmond, Virginia 23218

Dear Ms. Mavredes:

We have reviewed your audit report for Department of Veterans Services for the 30 month period ended December 31, 2014 and the Veterans Services Foundation for the 18 month period ended December 31, 2014. We appreciate the acknowledgment of proper recording and reporting of all transactions, in all material respects, in the agency financial system.

We concur with your findings and recommendations with regard to increased internal controls and matters that are required to be reported. We began addressing some of these issues as the audit was being conducted.

With regard to the Comment to Management: Evaluate Payroll Controls and Capabilities before Terminating Service Agreement: DVS has already evaluated agency staffing and has determined that we possess the capabilities to develop and implement the functions and controls currently being provided by the Bureau. All payroll/leave positions that were in place prior to conversion to the Bureau are still in existence and the employees holding them are fully capable of resuming their duties. We have advised our payroll/leave staff they need to ensure they are up to date on the latest "CIPPS/data entry" guidelines since there have been updates and new options added since we processed our payroll in house.

The decision has been made that DVS will resume processing our own agency Payroll/leave and David Von Moll, State Comptroller has agreed. Jean Turlington, PSB Director and Tammy Davidson, DVS Director of Finance had an initial conversation and have agreed the end of calendar year 2015 is the logical transfer date. DVS will resume processing their own payroll and leave accounting effective 12/25/15. The PSB has a detailed exit strategy they have developed and we will utilize to successfully accomplish the transition. We are prepared and fully capable of resuming these duties and will work with the Bureau to ensure a smooth transition.

AN EQUAL OPPORTUNITY EMPLOYER
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Ms. Mavredes
October 21, 2015
Page 2

We will file the required corrective action plan with the State Comptroller within 30 days of receipt of our official APA audit report. We thank you and your staff for your review and the assistance you have provided us.

Sincerely,



John L. Newby II

AGENCY OFFICIALS

As of December 31, 2014

John L. Newby II
Commissioner

Tammy Davidson
Director of Finance